COMMONWEALTH OF VIRGINIA

STATE CORPORATION COMMISSION

AT RICHMOND, MAY 26, 1999

COMMONWEALTH OF VIRGINIA

At the relation of the

STATE CORPORATION COMMISSION

CASE NO. PUE990349

Ex Parte: In the matter concerning the participation of incumbent electric utilities in regional transmission entities

ORDER ESTABLISHING INVESTIGATION AND INVITING COMMENTS

Introduction

The Virginia Electric Utility Restructuring Act, 56-576 et seq., (hereinafter, "the Act") will fundamentally alter the electric industry in Virginia by providing for retail choice in the purchase of electric energy. The Act directs the Commission to begin retail choice on or before January 1, 2002 for some customers, and to make such choice available to all customers by January 1, 2004.[1]

The Act recognizes that a prerequisite to retail choice and competition is nondiscriminatory access to a reliable transmission grid that is planned and operated on an efficient, neutral basis. To that end, the Act contains important obligations and authorities for the utilities and the Commission, relating to the planning, operation and pricing of transmission facilities. The major provisions are as follows:

Section 56-577 A.1 provides:

> On or before January 1, 2001, each incumbent electric utility owning, operating, controlling, or having an entitlement to transmission capacity shall join or

[1] The Commission may accelerate or delay this implementation, up to January 1, 2005, based on considerations of reliability, safety, communications or market power.

> establish a regional transmission entity, which entity may be an independent system operator, to which such utility shall transfer the management and control of its transmission system, subject to the provisions of § 56-579.

Section 56-576, in turn, defines an "independent system operator" to be "a person that may receive or has received, by transfer pursuant to this chapter, any ownership or control of, or any responsibility to operate, all or part of the transmission systems in the Commonwealth."

Section 56-579 furnishes the standards with which the incumbent electric utility must comply in carrying out its obligation to join or establish an RTE. It also vests in the Commission the obligation and authority to ensure that compliance. Specifically, § 56-579 A.1 provides that the incumbent electric utility shall not "transfer to any person any ownership or control of, or any responsibility to operate, any portion of any transmission system located in the Commonwealth without obtaining the prior approval of the Commission."

Section 56-579 A.2 directs the Commission to develop rules and regulations under which any incumbent utility may transfer all or part of any control, ownership or responsibility to an RTE. These rules and regulations must ensure that the transfer will:

> a. Promote:
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> (1) Practices for the reliable planning, operating, maintaining, and upgrading of the transmission systems and any necessary additions thereto; and
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> (2) Policies for the pricing and access for service over such systems, which are safe, reliable, efficient, not unduly discriminatory and consistent with the orderly development of competition in the Commonwealth;
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> b. Be consistent with lawful requirements of the Federal Energy Regulatory Commission;
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> c. Be effectuated on terms that fairly compensate the transferor; [and]

> d. Generally promote the public interest, and are consistent with (i) ensuring the successful development of interstate regional transmission entities and (ii) meeting the transmission needs of electric generation suppliers both within and without this Commonwealth.

Section 56-579 B further directs the Commission to:

> [A]dopt rules and regulations, with appropriate public input, establishing elements of regional transmission entity structures essential to the public interest, which elements shall be applied by the Commission in determining whether to authorize transfer of ownership or control from an incumbent electric utility to a regional transmission entity.

Section 56-578 F grants the Commission direct authority to require additional transmission facilities and to carry out other obligations. Specifically, this provision states that:

> If the Commission determines that increases in the capacity of the transmission systems in the Commonwealth, or modifications in how such systems are planned, operated, maintained, used, financed or priced, will promote the efficient development of competition in the sale of electric energy, the Commission may, to the extent not preempted by federal law, require one or more persons having any ownership or control of, or responsibility to operate, all or part of such transmission systems to:
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> 1. Expand the capacity of transmission systems;
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> 2. File applications and tariffs with the Federal Energy Regulatory Commission (FERC) which (i) make transmission systems capacity available to retail sellers or buyers of electric energy under terms and conditions described by the Commission and (ii) require owners of generation capacity located in the Commonwealth to bear an appropriate share of the cost of transmission facilities, to the extent such cost is attributable to such generation capacity;
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> 3. Enter into a contract with, or provide information to, a regional transmission entity; or
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> 4. Take such other actions as the Commission determines to be necessary to carry out the purposes of this chapter.

Section 56-579 C directs the Commission to participate before FERC in any and all proceedings concerning regional transmission entities furnishing transmission services within the Commonwealth, to the fullest extent permitted by federal law. Such participation may include such intervention as is permitted state utility regulators under FERC rules and procedures.

Also, § 56-579 F directs the Commission to report to the Legislative Transition Task Force[2] its assessment of RTE practices and policies as they relate to the orderly development of competition within the Commonwealth. This report is due on or after January 1, 2002.

Given the regional nature of the transmission grid and the institutions being formed to manage it, this Commission is not the only forum addressing these issues. Other states, acting under new statutes or under pre-existing authorities, are examining their jurisdictional utilities' use of transmission and their plans (or lack thereof) to join a particular regional transmission group. Moreover, FERC, in Order No. 888,[3] issued eleven general principles applicable to proposals for independent system operators. FERC also issued a Notice of Proposed Rulemaking (hereinafter, "NOPR")[4] this month which, among other things, asks whether the eleven principles need further definition. The Commission will participate actively in FERC's deliberations as envisioned by the Act. Similarly, our jurisdictional utilities participate in discussions with other utilities and other states, and in FERC proceedings. However, this

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[2] This is a task force to be established pursuant to § 56-595 to work collaboratively with the Commission in conjunction with the phase-in of retail choice in the Commonwealth.

[3] See Promoting Wholesale Competition Through Open Access Non-discriminatory Transmission Services by Public Utilities and Recovery of Stranded Costs by Public Utilities and Transmitting Utilities, 61 Fed. Reg. 21,540 (1996), FERC Stats. & Regs. ¶ 31,036 (1996) (Order No. 888), order on reh'g, Order No. 888-A, 62 Fed. Reg. 12,274 (1997), FERC Stats. & Regs. ¶ 31,048 (1997), order on reh'g, Order No. 888-B, 62 Fed. Reg. 64,688, 81 FERC ¶ 61,248 (1997), order on reh'g, Order No. 888-C, 82 FERC ¶ 61,046 (1998), appeal docketed, Transmission Access Policy Study Group, et al. v. FERC, Nos. 97-1715 et al. (D.C. Cir.).

[4] Regional Transmission Organizations, Notice of Proposed Rulemaking, Docket No. RM99-2-000, 87 FERC ¶ 61,173 (issued May 13, 1999).

Commission and Virginia's utilities have obligations under the Act which must be carried out as well. These obligations must also be integrated with discussions and proceedings in other jurisdictions. Wherever appropriate in the context of a particular question, we invite comments on what actions the Commission and the utilities can take to achieve this integration.

For example, in specifying the criteria by which we will evaluate our utilities' compliance with their state law obligations, we will need to address the intersection between those criteria and FERC's eleven ISO principles. Given the many industry developments in the three years since FERC issued those principles, some have questioned whether they provide sufficient guidance and incentive to facilitate the formation of effective RTEs, including RTEs involving Virginia utilities, as industry change evolves. FERC itself has called for a reevaluation of the principles in its recent NOPR proposing minimum characteristics and functions that transmission entities must satisfy to be deemed regional transmission organizations ("RTOs"). Consequently, in responding to each question below, we seek comment on how the Commission might best integrate its own rules and regulations on RTEs with those issued by FERC.

In accordance with these various mandates, the Commission is initiating this proceeding to assist in developing appropriate policies, rules and regulations applicable to the utilities' obligations to join or establish RTEs, to the transfers of facilities or control thereof to RTEs, and to the Commission's powers to require expansions in transmission facilities, and to carry out its other responsibilities under Section 56-578 F.[5]

The order also discusses potential policies and criteria, and seeks public comment on, a variety of issues. These issues fall roughly into the following categories:

I. Governance

[5] These comments will also aid the Commission in fulfilling its obligations under the Act to participate in all Virginia-related RTE proceedings before FERC.

II. RTE Activities

III. Geographic Scope and Access to Markets.

IV. Pricing

V. Relationship Between RTE Service and Bundled Retail Service

VI. Legal Issues

VII. Other Issues

VIII. Measuring Success

Comments should be specific, detailing the roles to be played by the Commission, the utilities and other participants in the formation of RTEs. To the extent possible and practicable, interested parties should include with their responses to this order proposed rules and regulations corresponding to comments on the issues set forth in this order. Such concrete proposals will assist the Commission in accomplishing the goals of this proceeding.[6]

Following a thorough review of the responses to this order, including suggested rules and regulations, we will propose specific rules and regulations under the Act, seek further public comment, and conduct further proceedings.

I.
Governance

A. Independence

To assure independent, neutral operation, an appropriate RTE structure should, at a minimum, reflect the paramount requirements of the Act: full functional separation of the transmission and generation functions of incumbent utilities, and nondiscriminatory access for all

[6] To aid the Commission as well as responding parties, each request for comments is numbered and set forth in bolded text. The parties are requested to correlate their responses to the numbering system set forth in this order.

market participants. The extent of independence is a function of the RTE's governance and structure.

Independence can be sought through various means including standards of conduct, RTE structures, advisory boards, etc. **[1] Generally, we seek comment on how RTE independence can best be achieved. [2] We also seek comment on a number of specific issues including what codes of ethics and/or conflict of interest rules should be applied to RTEs, their governing bodies, members and market participants.**

One structural option is a stakeholder board whose design limits the ability of any market segment to control transmission-related decisions. An alternative option is a nonstakeholder board, whose members have no interest in the competitive provision of electricity. Although greater independence of the board should have a positive effect on competition, we recognize that prescriptiveness may discourage voluntary participation in an RTE by utilities not subject to the Virginia statutory mandate. **[3] Consequently, we ask parties to comment on the appropriateness of requiring stakeholder boards (where no single market segment can inappropriately influence transmission access), or disinterested boards, as an essential element of an appropriately structured RTE. If such boards are considered appropriate, we ask interested parties to describe recommended governance requirements and to discuss how such requirements can be put in place.**

Potential alternatives or supplements to stakeholder or disinterested boards could include requirements for advisory boards which provide for representation from various market segments, state regulators, and consumer advocacy groups. **[4] We seek comment on the optimum structure of boards and a discussion of appropriate applications and structures of RTE advisory boards.**

The Midwest ISO has developed certain rights for transmission owners that allow the transmission owners to, in effect, veto or override decisions made by the ISO. The Alliance Regional Transmission Organization (hereinafter, "the Alliance"), a potential transmission entity that is being considered by Virginia Power, American Electric Power and other utilities, is considering similar "must haves" for transmission owners.[7] These requirements could afford transmission owners control or influence, to an extent not available to other stakeholders, over key facets of regional transmission policy, including the addition of new transmission systems to an RTE, changes in rate design, tariff changes, asset sales, declarations of bankruptcy, and even the very decision to continue or terminate the arrangement. The Alliance proposal, which appears to require transmission owners' approval for changes to the transmission tariff, would be inconsistent with FERC's NOPR requirement that the RTO have the exclusive authority to file changes to its transmission tariff.[8] Some transmission owners defend these measures as necessary to protect their financial interests. The assurance of an opportunity to receive a transmission revenue stream sufficient to cover expenses and a reasonable return is, of course, a legitimate owner expectation. The methods for creating such assurance, however, can and must be consistent with the neutral planning and operation of the transmission grid. **[5] Therefore, we ask parties to comment on the appropriate extent of transmission owner rights and to what degree certain such features may be inappropriate.**

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[7] See the Alliance Steering Committee Minutes from March 8, 1999 Meeting, which may be accessed at the Alliance website, http://isoalliance.com.

[8] NOPR, at 120, 126-28.

B. Alternative RTE Structures

[6] We are also interested in whether certain RTE structures are inherently more effective than others and, if so, whether we should encourage or specify certain structures. In this regard, interested parties submitting comments should address the following issues:

[7] Does an RTE that owns transmission facilities (hereinafter, "a transco") and that has a profit-driven motivation have a greater incentive to control costs and operate efficiently than a nonprofit entity that simply controls transmission facilities owned by others, or does a transco have an incentive to construct excess facilities or otherwise act inefficiently?

[8] Would a stand-alone transco stimulate more innovation or present more opportunities for improving transmission delivery services in a competitive market?

[9] Does a stand-alone transmission entity such as an unaffiliated transco provide for greater independence than other entities?

If there are preferences for specific RTE structures, participants filing comments should address our legal authority to require or provide incentives for such structures, taking into account the Act and its interaction with the Federal Power Act.

As detailed in the Alliance's October 30, 1998 Proposal for Phase III, this RTE would potentially incorporate a hybrid organization that would both own transmission facilities and control transmission facilities owned by others. Such an entity could complicate issues associated with governance and independence, since it would have to recognize its fiduciary responsibilities to its shareholders, while also protecting the interests of entities owning transmission facilities under the RTE's control and users of transmission services. **[10] We ask interested parties to comment on whether an entity of this type requires special**

consideration or restrictions in connection with transferring transmission assets to such an entity, and, if so, to suggest appropriate measures to protect the public interest.

Sections 56-577 A.1 and 56-579 of the Code of Virginia obligate an incumbent electric utility to "join" or "establish" an RTE. Under Sections 56-576 and 56-577 A.1, an RTE can be "a person that may receive or has received, by transfer pursuant to this chapter, any ownership or control of, or any responsibility to operate, all or part of the transmission systems in the Commonwealth." This phrasing indicates that a utility might seek to establish, or might be required by the Commission to establish, a single-utility RTE**. [11] Commenters should address the circumstances under which the Commission should require or allow an incumbent utility to form a single utility RTE, as well as the circumstances under which the public interest would be served by a utility's membership in an RTE consisting of multiple utilities.**

C. Miscellaneous Issues

[12] What incentives for efficient management and administration of an RTE can and should be incorporated in an RTE structure?

[13] What specific complaint or dispute resolution systems should be employed by an RTE?

II.
RTE Activities

A. Reliability

The Act emphasizes the continuation of adequate and reliable service in Virginia. The responsibility for ensuring adequate and reliable service has traditionally been performed by vertically integrated utilities with state oversight. The Act did not alter the utilities' reliability

obligations, yet many view RTEs as having a role in ensuring reliability. **[14] We invite comment regarding the role RTEs should play in ensuring reliability, both short-term and long-term, how that role interacts with the utilities' continuing legal obligation to ensure reliability, and what role the Commission should play in this area.**

[15] More generally, commenters should address whether the goals of reliability and effective competition are mutually supportive, or whether there are tradeoffs between these two oft-stated goals. If compromises are necessary, how can they be identified and how can adverse effects be minimized and mitigated?

It would appear that there are several ways in which RTEs may assist in ensuring that overall reliability of the bulk power system is maintained. RTEs could potentially play a key role in the dissemination of information concerning the adequacy of generating resources. Although RTEs may not have a direct responsibility in requiring sufficient generating reserves, they should be uniquely situated to recognize deficiencies in the bulk power system. Knowledge gained through the day-to-day operation of transmission facilities can serve as an early warning of future problems. This knowledge, in conjunction with the long-term planning activity of RTEs, which necessitates consideration of future electrical loads and generation resources, may provide an overall view of the adequacy of bulk power systems that may not be readily available to retail consumers, distribution utilities and competing power suppliers. Accordingly, one essential element of an RTE could be the provision of reliability information through periodic public reports detailing projections of future loads, generating reserves and expected areas of transmission congestion. Such information could enable consumers and potential suppliers to make informed decisions with respect to expansion of production facilities, location of new generating resources, and other issues. **[16] We therefore seek comment as to whether the**

collection and dissemination of reliability-related information should be required as an essential element of an RTE serving Virginia and, if so, how such an element could be incorporated into our rules and regulations.

RTEs may also play a more direct role in assuring adequate generating reserves. For example, the PJM Interconnection, L.L.C. (hereinafter, "PJM ISO") administers a reserve sharing agreement that assigns each load serving entity an installed capacity obligation and assesses a capacity deficiency charge to any entity that fails to meet this obligation. Such a mechanism, providing regional oversight with respect to the adequacy of generating reserves, helps assure that the needs of a region are recognized and met. **[17] Commenters should address whether the Commission should require a reserve sharing agreement similar to that required by the PJM ISO as an essential element of our utilities' RTE obligations. We further request that the parties identify any other mechanisms that would provide effective regional oversight with respect to the adequacy of generating reserves.**

Another key responsibility of an RTE is the procurement and provision of certain ancillary services. Such services must, in most cases, ultimately be provided from generating units. Consequently, RTEs must either contract for such services or require that transmission users arrange for such services. Redispatch of generating units for transmission congestion relief requires similar arrangements. Such ancillary and redispatch services may be required from specific generating units at certain times in order to maintain reliable service.

The generation market is undergoing rapid change, including voluntary and mandatory divestiture, and the growing use of market pricing as a substitute for traditional cost-based pricing. The source and price of essential generation services is therefore becoming less predictable. The potential for market power abuse, through excessive charges for such services,

or outright refusal to provide them, exists. Generation owners may have an incentive to withhold the provision of ancillary and congestion relief services from key generating facilities in order to manipulate the market.

[18] Commenters should address whether membership in the RTE or transmission service to the owners of generating units located within the geographic boundaries of the RTE should be conditioned on interconnection agreements that obligate the owners of generating units to provide ancillary and redispatch services. If so, should the provision of ancillary and redispatch services be conditioned on rates that are fairly compensatory to the providers of such services?

B. Access to Information

[19] What principles should apply to the exchange of RTE information among RTE members, RTE users, regulators and the public? Additionally, what kinds of information should be made available for exchange, and what limits, if any, should be imposed on such exchanges?

C. Construction of Transmission Facilities

The introduction of RTEs creates a need to clarify responsibility for construction of transmission facilities. The incumbent utility historically has had responsibility for planning and implementing reinforcements of the transmission grid. The Act did not change this responsibility. However, the goal of neutral, efficient transmission planning might require the RTE to assume some or all of these responsibilities. Thus, FERC has proposed that RTOs "should have ultimate responsibility for both transmission planning and expansion within its region."[9]

[9] NOPR at 189.

The possible desirability of the RTE having responsibility for construction raises practical concerns in a context in which state law traditionally has applied. For example, as a legal matter, an RTE might be dependent on one or more incumbent utilities to seek state permission to construct the facilities and to undertake actual construction. It may not always be in a particular utility's financial interests, however, to carry out the RTE's construction priorities; for example, where the construction of a new transmission facility would result in reduced utilization of the incumbent utility's generating facilities.

Given these concerns, parties should respond to the following questions:

[20] Should RTEs have direct authority, upon obtaining appropriate regulatory approvals, to construct needed facilities?

[21] Alternatively, or in addition, should RTEs have authority to require assurances from the utility transmission owner that the utility will, in good faith, undertake a diligent effort to secure all necessary approvals for the needed facilities? What would be the enforceable legal mechanism by which such assurances would be sought and obtained? Should an RTE have enforcement authority -- and what type -- if the utility did not make a good faith effort to obtain such approvals? If interested parties believe that such requirements are appropriate, we request comments suggesting proposals for specific provisions and how such provisions can be implemented and enforced by RTEs.

D. Planning of Transmission Facilities

The planning activities of an RTE could potentially influence competitive developments. For example, a new transmission facility, that may not be needed to maintain reliability or system security, could facilitate greater access to competitive generation markets. Such a facility could be cost effective if the economics of generation and transmission are both considered.

However, such joint consideration might not be within the responsibility of an RTE if the RTE's responsibilities were limited to reliability only.

More generally, the advantages of jointly considering generation and transmission economies should not be lost as certain transmission functions migrate from the utility to the RTE. **[22] Consequently, we are interested in whether the planning activities of an RTE can be conducted in a manner that will retain these vertical economies, and we ask parties to comment on appropriate planning considerations of an RTE. Specifically, interested parties should address whether the impact of proposed transmission facilities on access to competitive generation markets should be considered in the planning process and, if so, how.**

E. Operation of Transmission Facilities

[23] We also seek comment regarding whether our rules and regulations should detail the specific operating characteristics of an ISO as elements of an RTE. Consider the following examples, among others:

The Midwest ISO Agreement, which has received conditional authorization from FERC, specifies that the transmission owners who are currently control area operators will continue to operate their control areas for local generation control and economic dispatch purposes. This approach raises a potential concern that transmission owners will have a competitive advantage relative to those participants that do not operate control areas. Critics of the Midwest ISO have cited the following four problems: (1) control area operators will have knowledge of all schedules and transactions involving participants in their control areas; (2) control area operators' authority over other participants will allow them to take actions, purportedly for system reliability, that could put other participants at a competitive disadvantage; (3) control area

operators will not pay load imbalance penalties because they will have access to inadvertent energy accounts that would allow them to pay back positive and negative imbalances in kind, while noncontrol area participants would have to pay these penalties; and (4) control area operators will be able to obtain the economic benefits of the imbalance diversity of individual customers within that geographic area.

[24] Given the prospect that differing RTEs may have varying levels of operational control, we ask interested parties to comment on whether it would be appropriate to promulgate minimum requirements with respect to the operational responsibilities of an appropriately structured RTE, such as directing that the RTE serve as a single control area or requiring that each utility's control area functions be transferred to a separate independent entity, or that all of a utility's control area activities be subject to the control of an independent RTE. If such minimum requirements are appropriate, interested parties should describe in detail appropriate requirements and discuss how such requirements may be implemented.

F. Market Power Monitoring

We discussed above an RTE's unique ability to gather and disseminate reliability-related information. Similarly, RTEs may be a valuable resource with respect to identifying market power abuses. **[25] Accordingly, we will consider the advisability of requiring the submittal of information regarding proposed RTE market monitoring activities in related filings before this Commission, and we invite comments on this possibility. Such information should describe in detail (i) the type and frequency of information to be collected, (ii) the confidentiality and public availability of such information, and (iii) how such information**

could be provided to the Commission. We also ask for comment on the role RTEs should play, if any, in preventing or penalizing market power abuse.

G. Environmental Issues

While we believe that existing requirements for the construction of new transmission systems clearly require the consideration of the environmental impact of such facilities, we ask interested parties to comment on the advisability of other environmental considerations.

For example, an RTE could help facilitate clean air considerations by assuming responsibility for collecting information on power plant emissions associated with system dispatch and making such information available to the public. Such a function is being performed by ISO New England, which collects information associated with the system and provides historical emissions data concerning the New England region, relative to the percentage of coal, gas, and oil-fired generation, to the Massachusetts Department of Telecommunications and Energy. The Department of Telecommunications and Energy then coordinates that data with data from the Environmental Protection Agency and the Massachusetts Department of Environmental Protection on emissions levels. The ISO also provides the percentage generation data to load serving entities for presentation on "labels" that must accompany power bills in that state. **[26] We ask interested parties to comment on the appropriateness of requiring similar measures for RTEs operating in Virginia. If such measures are believed to be proper, we ask that commenters fully describe recommended requirements and their statutory basis.**

III.
Geographic Scope and Access to Markets

The geographic scope of an RTE has implications for transmission efficiency, reliability, operational practices, and other issues. More broadly, the geographic scope of an RTE and its pricing of transmission services may define or influence generation markets. **[27] We ask parties to comment on whether our RTE considerations should seek to balance the benefits associated with greater access to functioning generation markets and transmission efficiencies? If so, commenters should detail specific approaches for balancing these objectives.**

In this context, comments should address the subject of what might be the appropriate geographical scope and coverage of an RTE. Specifically:

[28] What should be the characteristics of the RTE's authority over control area operations within the RTE area? How will geographic size and coverage affect system constraints within the RTE and among the RTE and neighboring transmission owners or RTEs? How should an RTE coordinate with neighboring RTEs, control areas and utilities? What specific authority will be needed to accomplish these objectives?

[29] We also seek comments concerning the desirability and utility of RTEs which consist of, or include, noncontiguous transmission systems or systems with limited interchange capability among functioning power markets.

[30] Additionally, we invite comment on whether the Commission should favor RTEs which increase or improve interchange capability among functioning power markets.

IV.
Pricing

The development of effective competition may also be dependent on the pricing policies of an RTE. FERC's third ISO principle provides that an ISO should provide open access to the transmission system and all services under its control at nonpancaked rates pursuant to a single, unbundled, grid-wide tariff that applies to all eligible users in a nondiscriminatory manner. FERC, however, has departed from this principle. For example, in its conditional authorization of the Midwest ISO, FERC has allowed for multiple zonal rates. While the Midwest ISO effectively eliminates rate pancaking, customers in different zones may pay different transmission rates.

Other proposals, such as one from Alliance, may suggest further departure from FERC's pricing principles. It appears that the Alliance proposal would not eliminate transmission rate pancaking, since it provides for regional access charges in addition to zonal transmission charges. It should be noted that this proposal is designed to assure that no single transaction will be subject to higher costs than would be incurred under existing open access tariffs. We understand that the RTO envisioned by the Alliance proposal would switch to a single, grid-wide transmission rate at the end of a transition period. We are concerned that, while eliminating pancaked rates can enhance competition, the change may entail transmission cost shifts. The acceptability of such cost shifts may depend on whether there are countervailing benefits, such as increased reliability or enhanced access to lower cost power supplies.

In light of the foregoing discussion, we believe that it is appropriate to examine closely whether RTE pricing policies result in the elimination of pancaked rates and whether proposals for implementing a single grid-wide rate are appropriate. These considerations could play an important role in any evaluation of a particular RTE. **[31] Accordingly, we ask interested**

parties whether it would be appropriate to require incumbent utilities seeking to transfer ownership or control of transmission facilities to an RTE to file detailed information showing how RTE pricing proposals will impact Virginia consumers. If so, parties should comment on the specific information that should be required.

In addition to pancaking and "single rate" issues, other pricing questions arise, particularly concerning the collection of congestion and variable costs. FERC's eighth ISO principle requires that transmission and ancillary service policies should promote efficient consumption and efficient investment in generation and transmission facilities. FERC notes similar objectives for RTOs in its recent NOPR. We also wish to mitigate any loss in present planning efficiencies that may occur as a result of the functional separation of generation and transmission. **[32] Consequently, we seek comment regarding whether there are specific pricing elements that are essential to an appropriately structured RTE, and if so, ask that commenters identify these elements. For example, should our rules require, as an essential RTE element under the provisions of Section 56-579, locational marginal pricing for congestion relief, provisions for tradable transmission rights, or other such measures?**

V.
Relationship Between RTE Service and Bundled Retail Service

[33] We also seek comment regarding the impact of participation by Virginia jurisdictional utilities in any regional RTE operating in the Commonwealth on the service to customers receiving bundled retail services during the transition to retail choice and customers receiving default service after choice is available to all customers. Customers who do not have choice during the transition period or who, at any time subsequent to the commencement of retail choice, elect not to take service from alternative suppliers may continue to receive service, which, under certain circumstances, may be bundled service. FERC has

acknowledged that it has jurisdiction only over the rates, terms and conditions of unbundled transmission service provided by public utilities engaged in interstate commerce, not over bundled retail sales. Given that utilities participating in an RTE will be regulated concurrently by the federal and state governments, we are interested in comments addressing how RTE participation may impact our jurisdictional responsibilities and authority with respect to bundled retail services.

[34] In particular, we invite comments regarding whether RTE participation may alter the priorities of service to bundled retail customers and the rates for such services. In a recent decision, the United States Court of Appeals for the Eighth Circuit held that FERC, in its application of Order No. 888, acted beyond its jurisdiction when it required a transmission owner, in its provision of transmission service to unbundled transmission customers, to use curtailment procedures which are comparable to those which the transmission owner uses for its customers of bundled retail service.[10] **[35] We ask interested parties to comment on how the Court's ruling, if it were to apply in Virginia, might affect the permissible curtailment practices of an RTE, and what, if any, guidance this Commission should provide, particularly as that guidance might affect service to bundled retail load in Virginia. [36] In addition, should the curtailment provisions of RTEs recognize a higher priority of service to bundled retail loads? If so, identify considerations or propose appropriate curtailment provisions that should be incorporated into our rules.**

We are also concerned that FERC's ratemaking practices with respect to unbundled transmission service may differ from ours as applied to bundled transmission service, and that

[10] Northern States Power Co. v. FERC, __ F.3d __ (8th Cir. Mar. 8, 1999), 1999 WL 301458 at 4-5 (finding that the indirect effect of Order No. 888's curtailment procedures, as interpreted by FERC, constituted an attempt to regulate the curtailment of transmission service to retail customers, thus transgressing its Congressional authority which limits its jurisdiction to interstate transactions).

application of FERC approved rates for transmission services could result in differing revenue requirements for bundled retail services. **[37] Therefore, we ask interested parties to comment on whether our RTE related rules should establish specific considerations for reconciling state and federal ratemaking practices for bundled retail services. If such conditions are appropriate, we ask parties to propose specific provisions or rules for our consideration.**

VI.
Legal Issues

A. Treatment of an RTE Under State Law

[38] Contemplating the broader relationship between RTEs and the statutory and constitutional requirements of this Commonwealth,[11] we solicit comment on the following issues: (i) whether RTEs will perform a public service function in Virginia; and (ii) if so, whether an RTE should be considered a public service company or public utility under Virginia law. Commenters should address whether RTEs may be subject to Virginia corporate statutes and should be required to incorporate as a Virginia public service corporation. If commenters assert that Virginia statutes are inapplicable to RTEs, such comments should explain in detail, citing applicable law, the reasons why.

B. Carrying Out the State Legislature's Mandate In the Context of the Federal Power Act

As indicated in the introduction to this order, the Commission and its jurisdictional utilities must carry out the Act's RTE mandates in a legal context that includes activities of other

[11] See, Va. Const. art. IX, § 5, prohibiting foreign corporations from carrying on the business of, or performing the functions of, a public service enterprise within the Commonwealth.

states, and of FERC acting under the Federal Power Act. This multijurisdictional context raises both legal and practical issues.

Courts have interpreted the Federal Power Act to preempt state activities under certain circumstances. Commenters should point out, throughout their comments, areas where they believe the Commission's responsibilities concerning RTEs under the Virginia Act may be limited by federal law. Comments should be specific and make reference to judicial and statutory authorities.

From a practical perspective, there will be a need to coordinate our actions with FERC's, and those of other states, so as to recognize the multi-utility and regional nature of these issues while also carrying out the requirements imposed by our General Assembly. Again, commenters should point out, throughout their comments, areas in which coordination will be especially necessary, and identify means by which this coordination can occur.

VII.
Other Issues

A. Transmission-Distribution Distinction

[39] How should the distinction between transmission and distribution facilities be delineated, as a tool in identifying those facilities eligible for transfer to an RTE, or in defining facilities for inclusion in the investment bases of various companies? Are FERC's seven indicators concerning this subject appropriate for use in establishing essential RTE elements?

B. Ratemaking Implications of Transfers of Assets or Control

[40] Should the costs and proceeds associated with asset transfers be reflected in rates? Should we develop filing requirements for schedules detailing the

Virginia-jurisdictional ratemaking implications of RTE proposals? Commenters should describe fully the information that should be collected through such filing requirements.

C. Additional RTE functions or responsibilities.

RTEs may also have functions or responsibilities that are intended to facilitate considerations that are not directly related to maintaining reliability or to providing nondiscriminatory access. **[41] Therefore, we are interested in whether there are additional elements that should be required for an appropriately structured RTE**.

VIII.
Measuring Success

[42] With particular regard to the Commission's duty to report to the Legislative Task Force on the success of RTE development, what are some possible benchmarks by which success of an RTE can be measured in the future? Comments on this topic should set forth proposed rules related to the development and justification for such benchmarks.

[43] Finally, we urge all interested parties to address in their comments, any other issue or sets of issues concerning or affecting the Commission's responsibilities with respect to RTEs.

As we begin this critical chapter in Virginia's restructuring process, we ask and expect all participants to cooperate fully with Commission staff and the Commission in this proceeding.

NOW, upon consideration of the foregoing, the Commission is of the opinion and finds that this proceeding should be docketed and that interested parties should be permitted to file initial comments on the issues raised herein, as well as comments responsive to those initially filed. Accordingly,

IT IS ORDERED THAT:

(1) This matter shall be docketed and assigned Case No. PUE990349.

(2) On or before June 10, 1999, any party intending to file comments in conjunction with this order shall file notice of their intent to do so, filing an original and twenty (20) copies of such notice with the Clerk of the State Corporation Commission. Such notice shall be addressed to Joel H. Peck, Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218, and shall refer to Case No. PUE990349. On or before June 18, 1999, the Clerk shall prepare and make available for purposes of service required under paragraphs (3) and (4) hereafter, a list of all parties indicating their intent to file comments concerning this order.

(3) On or before June 29, 1999, any interested party may file an original and twenty (20) copies of initial comments with the Clerk on the issues and policies posed in this Order. To aid the Commission as well as responding parties, each request for comments is numbered and set forth in bolded text. The parties are requested to correlate their responses to the numbering system set forth in this order. Comments shall be addressed to Joel H. Peck, Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218, and shall refer to Case No. PUE990349. Interested parties shall also serve one (1) copy of their comments upon the Staff and other parties to this proceeding. The parties are also requested to furnish the Commission electronic copies of their initial comments, if practicable, via e-mail attachment addressed to nlowery@scc.state.va.us.

(4) On or before July 15, 1999, interested parties desiring to respond to the initial comments filed herein pursuant to Ordering Paragraph (2) shall file with the Clerk of the Commission at the address set forth below, an original and twenty (20) copies of their responses to the initial comments. To aid the Commission as well as responding parties, the parties are

requested to correlate their responses, to the extent practicable, to the numbering system set forth in the requests for comments contained in this order. Service upon the Clerk of the Commission shall be directed to Joel H. Peck, Clerk, State Corporation Commission, c/o Document Control Center, P.O. Box 2118, Richmond, Virginia 23218, and shall refer to Case No. PUE990349. Interested parties filing responses shall serve one (1) copy of said comments upon the Staff and other parties to this proceeding. The parties are also requested to furnish the Commission electronic copies of their response comments, if practicable, via e-mail attachment addressed to nlowery@scc.state.va.us.

(5) Copies of the initial and response comments shall be made available for public inspection from 8:15 a.m. to 5:00 p.m., Monday through Friday, at the State Corporation Commission, Document Control Center, First Floor, Tyler Building, 1300 East Main Street, Richmond, Virginia 23219. Persons desiring to obtain copies of the comments filed herein may order a copy of such comments from the Clerk of the Commission at the address set forth in Ordering Paragraph (3). Copies of such comments are available at a charge of $1.00 per page for the first two pages of the document, and a charge of $0.50 for each additional page.